

STATE OF NEW YORK
DIVISION OF TAX APPEALS

In the Matter of the Petition	:	
of	:	
STODDARD COMMUNICATIONS, INC.	:	
D/B/A SATELLITE COMMUNICATIONS	:	
for Revision of a Determination or for Refund	:	
of Sales and Use Taxes under Articles 28 and 29	:	
of the Tax Law for the Period September 1, 1979	:	
through February 29, 1984.	:	

DETERMINATION

In the Matter of the Petition	:	
of	:	
DANIEL STODDARD,	:	
OFFICER OF STODDARD COMMUNICATIONS, INC.	:	
for Revision of a Determination or for Refund	:	
of Sales and Use Taxes under Articles 28 and 29	:	
of the Tax Law for the Period September 1, 1979	:	
through February 29, 1984.	:	

Petitioner Stoddard Communications, Inc. d/b/a Satellite Communications, 45 Church Street, Freeport, New York 11520, filed a petition for revision of a determination or for refund of sales and use taxes under Articles 28 and 29 of the Tax Law for the period September 1, 1979 through February 29, 1984 (File No. 801778).

Petitioner Daniel Stoddard, officer of Stoddard Communications, Inc., 45 Church Street, Freeport, New York 11520, filed a petition for revision of a determination or for refund of sales and use taxes under Articles 28 and 29 of the Tax Law for the period September 1, 1979 through February 29, 1984 (File No. 801777).

A hearing was held before Joseph W. Pinto, Jr., Administrative Law Judge, at the offices of the Division of Tax Appeals, Two World Trade Center, New York, New York, on March 2, 1989 at 9:15 A.M., with all briefs to be submitted by May 19, 1989. Petitioners appeared pro se. The Division of Taxation appeared by William F. Collins, Esq. (Michael Glannon, Esq., of counsel).

ISSUE

Whether the sale of telephone equipment by the corporate petitioner was exempt from the imposition of sales and use taxes under Tax Law § 1115(a)(12), the so-called "manufacturer's exemption".

FINDINGS OF FACT

Petitioner Stoddard Communications, Inc. ("the corporation"), which did business as Satellite Communications, sold, installed and serviced private telephone systems during the period at issue. Petitioner Daniel Stoddard, president of the corporation, at the hearing of this matter, conceded that he would be personally liable for any sales and use taxes determined to be due from the corporation. Mr. Stoddard had previously worked for New York Telephone as an installer and an installation foreman. When other than regulated companies were allowed to sell and service telephone systems, he went to work for a company called Telecom Plus. Subsequently, he started his own company, Stoddard Communications, Inc., to sell, install, maintain and repair telephone equipment and was president of the corporation throughout the period at issue.

During the approximately four and one-half year period at issue, the corporation reported taxable sales of \$4,791,109.00.

On November 14, 1984, the Division of Taxation issued four notices of determination and demands for payment of sales and use taxes due, two against Stoddard Communications, Inc. d/b/a Satellite Communications for the periods September 1, 1979 through February 28, 1983 and March 1, 1983 through February 29, 1984 showing tax due of \$153,271.22 and \$62,135.05, plus penalty and interest, respectively, and two against Daniel Stoddard, as officer of the corporation, for corresponding periods and amounts.

Of the total tax deficiency asserted against petitioners of \$215,406.27 (\$153,271.22 for the period September 1, 1979 through February 28, 1983 plus \$62,135.05 for the period March 1, 1983 through February 29, 1984), petitioners conceded that some tax was due and paid the following: \$3,162.63 on disallowed nontaxable sales, \$3,494.54 on the purchase of materials used in capital improvements, \$11,555.51 from the corporation's sales tax accrual account, and \$2,146.80 on recurring purchases for the corporation's own use. The amount that remains in dispute, \$195,046.79, represents additional sales tax asserted to be due on the sale of telephone systems. The telephone systems were described by the auditor as the equipment, the wiring, the switchboards and other property required to establish telephone service. The corporation hooked the customer into the telephone company's lines so that petitioners provided the system only, while the telephone company provided the telephone service.

The audit workpapers detailed the calculation of the additional tax asserted due on the sale of telephone systems by petitioners as follows:

<u>Period Ending</u>	<u>Total Taxable Sales</u>	<u>Adjustment for Correct Tax Rate</u>	<u>Tax Due</u>
11/30/80	\$ 261,763	2%	\$ 5,235.26
2/28/81	47,527	2%	950.54
5/31/81	352,816	4%	14,112.64
8/31/81	293,713	4%	11,748.52
11/30/81	687,585	4 ¹ / ₄ %	29,222.36
2/28/82	200,947	4 ¹ / ₄ %	8,540.25
5/31/82	305,956	4 ¹ / ₄ %	13,003.13
8/31/82	350,432	4 ¹ / ₄ %	14,893.36
11/30/82	527,031	4 ¹ / ₄ %	22,398.82
2/28/83	331,027	4 ¹ / ₄ %	14,068.65
5/31/83	559,929	4 ¹ / ₄ %	23,796.98
8/31/83	256,698	4 ¹ / ₄ %	10,909.67

11/30/83	305,017	4 ¹ / ₄ %	12,963.22
2/29/84	<u>310,668</u>	4 ¹ / ₄ %	<u>13,203.39</u>
Total	\$4,791,109		\$195,046.79

The amounts shown under the column "Total Taxable Sales" were taken from the corporation's sales tax returns. Petitioners had treated all of the sales reported from September 1, 1980 through February 29, 1984 as subject to the so-called manufacturer's exemption under Tax Law § 1115(a)(12), and accordingly charged a lower tax rate.

In or about July 1980, the Taxpayer Services Division issued a "Notice", a copy of which was sent to the corporation, noting, in part, as follows:

"Effective September 1, 1980, the statewide sales and use tax rate on certain parts, tools, supplies used or consumed in production and services to tangible personal property used or consumed in production is reduced to 2%.

The reduced rate of sales and use tax applies to:

* * *

B. ...

2. Installing, repairing, maintaining or servicing telephone and telegraph central office equipment and station apparatus used directly and predominantly in receiving at destination or initiating and switching telephone or telegraph communication...."

Daniel Stoddard reviewed this notice with his accountant, Maurice Mauner, who then advised him that the lesser sales tax rate could be charged on the corporation's sales of telephone systems. The corporation had been charging the full sales tax rate on its sale of telephone systems prior to its receipt of this notice.

The Audit Report Log shows that on August 30, 1982, the auditor advised petitioners' accountant that the Division of Taxation did not agree to any of the reduced rates charged by the corporation on its sale of telephone systems and that he thought they should be charging the full sales tax rates. The accountant replied that he felt they were correct and that he could substantiate petitioners' position. Apparently, the auditor's position was not conveyed by Mr. Mauner to Daniel Stoddard who testified that "Mauner never, to my knowledge, never told Forman¹ or myself that we were charging tax incorrectly...."

Although Daniel Stoddard created a business that had multi-million dollar sales during the period at issue, he was not a sophisticated businessman. As noted in Finding of Fact "1", supra, his background was in the technical aspects of the telephone industry. His credible testimony was that he "collected what I believed to be the proper amount. I did not receive any guidance that it was wrong."

SUMMARY OF THE PARTIES' POSITIONS

¹Donald Forman was the vice president of the corporation.

The Division of Taxation argues that the production exemption from sales tax is for equipment that is involved in a production process where the ultimate product will be subject to sales tax. The exemption from sales tax for telephone central office equipment is for the purchase of such equipment by telephone companies that provide a monthly taxable telephone service of transmitting telephone calls over their lines. Petitioners contend, by contrast, that they collected the proper amount of sales tax on the sale of telephone equipment based on a reasonable reading of the notice sent to the corporation in or about July 1980 by the Division of Taxation. Petitioners further contend that the Division should have acted faster and more decisively, rather than allowing the corporation to unwittingly continue to collect the wrong amount of sales tax so that the disputed amount grew to the point that petitioner, once a viable corporation, went out of business.

CONCLUSIONS OF LAW

A. Tax Law § 1115(a)(12), in part, provides an exemption from sales and use taxes for "telephone central office equipment or station apparatus or comparable telegraph equipment for use directly and predominantly in receiving at destination or initiating and switching telephone or telegraph communication...."

B. 20 NYCRR § 528.13(f) provides, in part, as follows:

"Telephone and telegraph equipment. (1) Telephone and telegraph central office equipment and station apparatus, used

directly and predominantly in receiving at destination, initiating or switching telephone and telegraph communication is exempt, when such equipment and apparatus is purchased or leased by the vendor of such service for sale.

(2) The purchase or lease of equipment by a person subscribing to a telephone or telegraph service, which is comparable to telephone or telegraph central office equipment or station apparatus is not eligible for exemption.

Example 1: A telephone company purchases switchboards and handsets for installation at a subscriber's premises. Such purchases are exempt.

Example 2: An airline company purchases consoles which initiate, receive and switch telephone calls which are sent over telephone company lines. The consoles are not exempt, as they were not purchased by a telephone company in connection with a telephone service for sale."

C. Under the above-cited regulation, it is clear that petitioner corporation was not entitled to collect sales tax at a reduced rate on its sale of telephone equipment because it was not a vendor of telephone service for sale. This regulation is a reasonable elaboration of the statutory "manufacturing exemption". The rationale for this exemption is rooted in the desire to avoid the pyramiding of sales tax. Because the telephone service for sale is subject to sales tax, certain of the costs of providing telephone service, i.e. the purchase of telephone central office equipment by a telephone company, were exempted from sales tax.

D. It should be noted that, as a general rule, statutory exemptions from tax are strictly construed against the party claiming the exemption. The burden is upon petitioners to clearly establish their right to the exemption provided by Tax Law § 1115(a)(12) (Matter of Grace v. State Tax Commn., 37 NY2d 193, 196, 371 NYS2d 715, 718). In the face of the clear regulatory language, which is a reasonable interpretation of the statutory exemption, the notice,

described in Finding of Fact "7", supra, did not provide a basis for establishing the corporation's right to the exemption at issue. Further, at best, the notice concerned a reduced sales tax rate for "installing, repairing, maintaining or servicing" telephone central office equipment and not the sale of such equipment.

E. This case is very similar to a prior matter, Matter of Coradian Corporation f/k/a United Telecommunications Corp. (State Tax Commission, May 27, 1983). In that matter, the Commission determined that telephone central office equipment sold to and installed on the premises of a law firm was not exempt from sales and use tax under the statutory exemption at issue herein.

F. It should also be noted that the Division cannot be faulted for allowing the corporation to continue to collect the wrong amount of sales tax. As noted in Finding of Fact "8", supra, the auditor, early in the audit, stated his disagreement with the corporation's use of the reduced sales tax rate to the corporation's accountant. The Division cannot be blamed for the apparent failure of the corporation's accountant to convey such information to Mr. Stoddard.

G. Petitioners established that they acted in good faith and that their failure to collect the proper amount of sales tax on the sale of telephone equipment was not willful. In light of the experience, knowledge and education of petitioner Daniel Stoddard, his reliance on his accountant's analysis of the notice, supra, provides an adequate basis for the abatement of penalties and interest in excess of the minimum.

H. The petitions of Stoddard Communications, Inc. d/b/a Satellite Communications and of Daniel Stoddard, as officer of Stoddard Communications, Inc., are granted to the extent noted in Conclusion of Law "G", supra, but, in all other respects, are denied.

DATED: Troy, New York
December 14, 1989

/s/ Joseph W. Pinto, Jr.
ADMINISTRATIVE LAW JUDGE